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Pooling-of-interests accounting

United States. Securities and Exchange Commission

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For RELEASE Friday, September 29, 1972

SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

SECURITIES ACT OF 1933
Release No. 5312

SECURITIES EXCHANGE ACT OF 1934
Release No. 9798

PUBLIC UTILITY HOLDING COMPANY ACT OF 1935
Release No. 17712

INVESTMENT COMPANY ACT OF 1940
Release No. 7395

ACCOUNTING SERIES
Release No. 130

Pooling-of-Interests Accounting

In recent months, the Commission has noted an increasing number of business combinations which appear to meet the individual requirements for pooling-of-interests accounting set forth in Accounting Principles Board Opinion No. 16 but which do not conform with the overriding thrust of that Opinion which requires that a combination represent a sharing of rights and risks among constituent stockholder groups if it is to be a pooling of interests. Paragraphs 28, 45 and 47 of that Opinion clearly provide that such a sharing of risk is an essential element in poolings, and the specific requirements set forth in paragraphs 46, 47 and 48 should certainly not be construed as a formula which, if followed with precision, may be used to overcome an essential concept which underlies the entire Opinion. Despite the clarity of the Opinion in articulating the need for a sharing of risk, a number of registrants and their auditors have proposed to account for combinations which did not meet this basic requirement as poolings.

Accordingly, the Commission has concluded that any confusion regarding this matter should be laid to rest. It is the Commission's understanding that the Accounting Principles Board has authorized its staff to issue an interpretation providing that a business combination should be accounted for as a purchase if its consummation is contingent upon the purchase by a third party of any of the common stocks to be issued. Including such a contingency in the arrangement of the combination, either explicitly or by intent, would be considered a financial arrangement which is precluded in a pooling under Opinion 16.

The Commission endorses this interpretation. Recent questions by registrants indicate that maximum prompt exposure should be given to this interpretation and to the Commission's policies for dealing with questions which arise under it both in the interim period during which the interpretation is being assimilated by the financial community and on a continuing basis thereafter.

As a matter of policy, the Commission believes that it is unwise to set forth absolute rules in such an accounting matter which will be followed regardless of all other factual situations which may surround a particular transaction. To do so would be to encourage the application of form over substance. Nevertheless, it appears reasonable for the Commission to establish guidelines which it will use in making determinations as to disposition of various individual cases brought before it and to make these guidelines known to registrants and independent public accountants.

In the case of business combinations, the Commission will consider that if a registration statement is filed contemplating the sale of stock issued in a combination which does not include at the date of filing a set of financial statements reflecting the completed transaction (including some period of combined operations), that fact will constitute prima facie evidence that the sale was included explicitly or by intent in the arrangement of the combination and, hence, pooling treatment is not appropriate. In other words, all stock issued in a pooling must be held at risk at least as long as it takes to prepare post-merger financial statements for the combined entity and then to file and await effectiveness of a registration statement before it can be publicly sold.

This release is not intended to restrict sale of stock at the option of the stockholders subsequent to the pooling as long as a sharing of risks for the period of time indicated above has taken place. An arrangement to register shares subsequent to the combination would therefore not bar pooling. However, an agreement which requires sale of shares after such a period would preclude pooling treatment as would any agreement to reduce the risk borne by the stockholders subsequent to the transaction.

During an interim period of 75 days while this release and interpretation are being assimilated and where transactions previously negotiated are being filed with the Commission, it seems reasonable to apply a less rigorous risk-sharing test while at the same time recognizing that in the Commission's general view a transaction in which no risk is shared is not appropriately treated as a pooling. During this interim period, therefore, the Commission will raise no questions as to the appropriateness of pooling accounting in transactions where at least 25% of the stock issued in the pooling is retained at risk by shareholders of the pooled company and where effective date of any registration statement covering sale of the stock to be sold is subsequent to the date the combination is consummated.

By the Commission

Ronald F. Hunt
Secretary